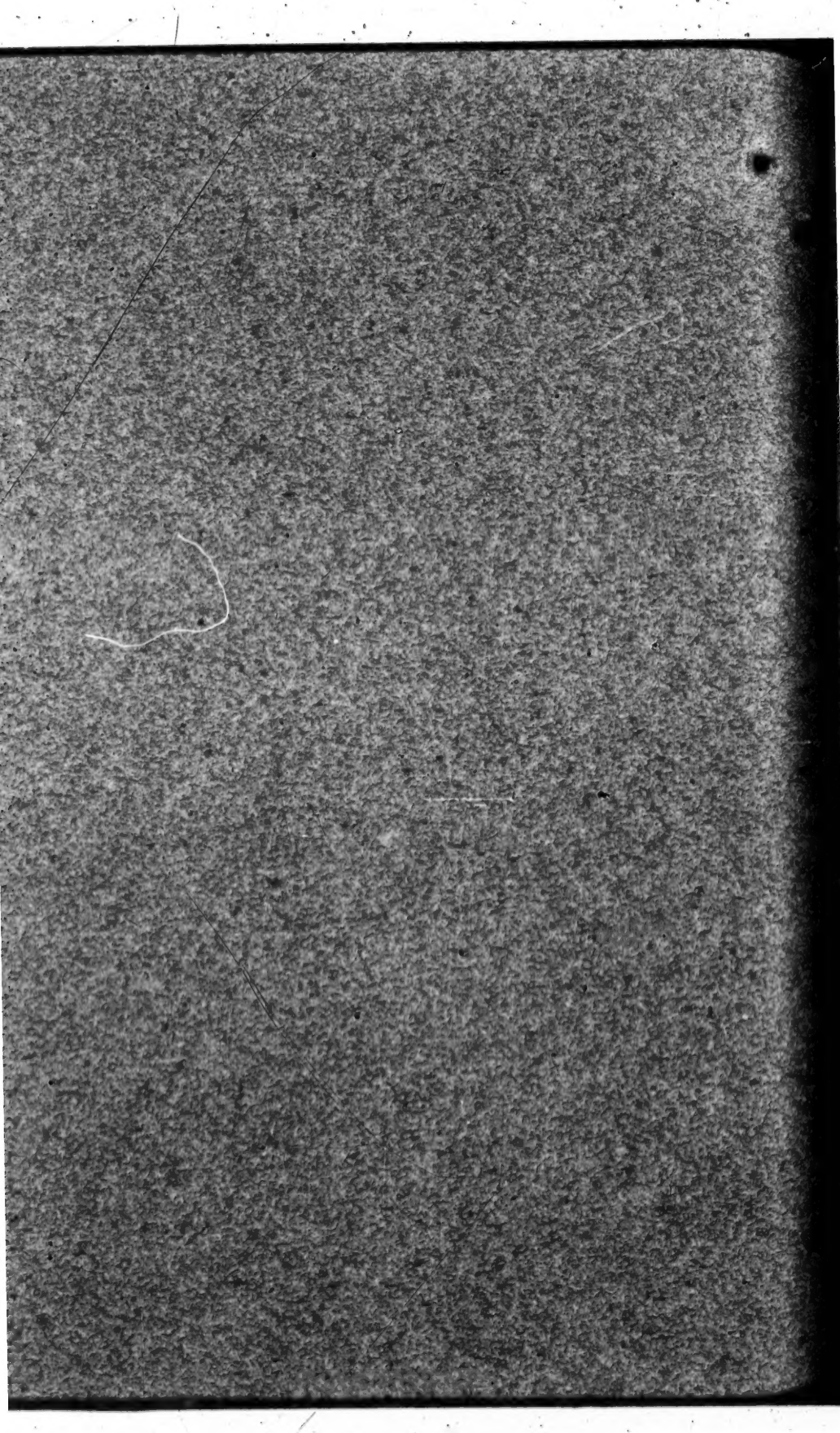

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No. 129

In the Supreme Court of the United States

OCTOBER TERM, 1930

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

SYBIL WHITEHOUSE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE PETITIONER

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OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 14) is reported in 7 B. T. A. 600. The opinion of the Circuit Court of Appeals for the First Circuit (R. 38) is reported in 38 F. (2d) 162.

JURISDICTION

The decree of the Circuit Court of Appeals was entered on February 17, 1930. (R. 42.) The petition for a writ of certiorari was filed May 17, 1930. Certiorari was granted on October 13, 1930. (R. 42.) The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether an annuity paid in instalments out of the income of an estate under a will which does not direct how the annuity shall be paid is taxable as income to the recipient under the provisions of Section 213 (a) and/or Section 219 of the Revenue Act of 1921, or to state it another way, whether such payments are exempt from tax as a bequest under Section 213 (b) (3) of that Act.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in Appendix A, *infra*, pp. 29–33.

STATEMENT

James Gordon Bennett died on May 24, 1918, leaving a last will and testament, the material provisions of which are set forth in the record. (R. 10–13, 28–32.) Under the will the testator provided for a number of annuities to be paid to various individuals, including the respondent. The terms of the will relating to the annuity in question, are as follows (R. 10):

> Tenth. I also give and bequeath to the said Sybil Douglas, wife of William Whitehouse, an annuity of five thousand dollars.

The will further provided (R. 29):

> All the above annuities mentioned in paragraphs ten to twenty-five of this my will shall be paid in equal semiannual payments, reckoning from the time of my death.

In paragraph twenty-nine of the will the testator stated that it had long been his intention and purpose to establish a substantial and permanent memorial to his father, the founder of the New York Herald. (R. 11, 30.) To carry out this intention the will provided that the testator's executors should incorporate a corporation to be named "The James Gordon Bennett Memorial Home for New York Journalists." (R. 11, 30.) The general objects and purpose of the corporation were to provide and maintain a suitable and comfortable home or to provide pecuniary aid for persons who had been employed by newspapers in the Borough of Manhattan, City of New York, and who should become incapacitated or in need of assistance. (R. 11, 30.) The will devised and bequeathed all of the residue of the estate of the testator to this corporation. All the income of the residuary estate prior to the formation of the corporation was given and bequeathed to Eugene Higgins, Rodman Wanamaker, and James Stillman. (R. 31.) These three men were also named as executors. (R. 32.)

The will further authorized the sale of any property for the payment of debts and of annuities and further provided as follows (R. 32):

> I authorize and empower said executors or executor to retain and hold any personal property which may belong to me at the time of my death and to set aside and hold any part thereof to provide for the payment and satisfaction of any annuity given by me.

The annuity provided for the respondent was paid to her in 1921 by the executors of the will of the testator out of the *income* of the estate. (R. 13.)

In November, 1921, the executors filed in the Surrogate's Court for the County of New York an intermediate account of settlement, which was thereafter approved by the court. The account showed that all of the annuities paid to the taxpayer and certain other annuitants were, prior to November 14, 1920, paid out of the corpus of the estate and those paid subsequently thereto were paid out of income. (R. 13.)

The account of settlement also shows that on December 30, 1920, the executors permanently set aside to the James Gordon Bennett Memorial Home for New York Journalists Corporation, but subject to taxes, annuities, and other charges, securities to the value of $3,133,260.00. (R. 14.)

SPECIFICATION OF ERROR TO BE URGED

The Circuit Court of Appeals erred in holding that the annuity paid during 1921 was exempt as a bequest under Section 213 (b) (3) of the Revenue Act of 1921, and in refusing to hold that the payment was taxable income within the meaning of Sections 213 (a), 219 (a), and 219 (d) of the Revenue Act of 1921.

SUMMARY OF ARGUMENT

I. In *Irwin* v. *Gavit*, 268 U. S. 161, this Court held that a gift of the income from a trust fund for

life, the beneficiary having no interest in the corpus, was taxable to the beneficiary under the Revenue Act of 1913 and was not exempt from tax as a bequest under that Act. Similar principles were applied in *Heiner* v. *Beatty*, 17 F. (2d) 743 (C. C. A. 3d), affirmed *per curiam*, 276 U. S. 598. The exemption provision in Section 213 (b) (3) of the Revenue Act of 1921, here involved, is in substance and effect the same as that involved in those cases.

In view of the fact that annuities are paid primarily from income, that the decedent left a residuary estate which would produce sufficient income for the payment of the annuities and that the payments taxed were in fact paid from income of the estate, it can not be said that the bequest was one of corpus. Hence the annuity is taxable under the decision of *Irwin* v. *Gavit, supra.*

The intention of Congress not to permit any of the income of an estate or trust to escape taxation is even clearer under the Revenue Act of 1921 than under the Revenue Act of 1913 construed in the *Gavit case.* Section 219 of the Act of 1921 specifically requires the trustee or executor to pay a tax on income received by him for the trust or the estate in certain cases and requires the beneficiary to pay the tax in other cases and this section when read in connection with Section 213 was intended to reach all income. Section 213 (b) (3) of the Revenue Act of 1921 must, therefore, be construed in conjunction with Section 219, with which it is *in pari materia.* The latter section makes the taxes

imposed by Sections 210 and 211 applicable to the income of estates of deceased persons during the period of administration and also to the income of estates and trusts which is to be distributed periodically, whether or not at regular intervals. It constitutes the estate or trust a separate taxable entity but requires the beneficiary to pay the tax on the portion of the income actually distributable to him. So far as the beneficiary is concerned, the test of taxability is whether there is distributable to him the net income of an estate or trust. *Riker* v. *Commissioner*, 42 F. (2d) 150 (C. C. A. 2d).

The Board of Tax Appeals and the Circuit Court of Appeals, in refusing to apply the principles of *Irwin* v. *Gavit*, and *Heiner* v. *Beatty* to the instant case, have distinguished between the case of a life beneficiary under a trust fund established under a will and a beneficiary receiving an annuity for life from a residuary estate. That technical distinctions between "bequests of income" and annuities are made is conceded, but these distinctions are of form, not of substance. In substance there is no distinction between income paid in one form or in another.

If the existence of a particular fund does make a difference, it is pointed out that the annuity which has been taxed here was paid from the particular fund established December 30, 1920, when the executors permanently set aside to the residuary devisee and legatee certain assets in the amount of $3,133,260, *subject to taxes, annuities, and other*

charges. The will impliedly gave the executors authority to make any provision for the payment of annuities which they deemed advisable.

But the question of taxability of income distributed to a beneficiary of an estate does not depend upon the existence of a fund, for in its absence the entire residuary estate is a fund in which the beneficiary has an interest. Moreover, payments of income may be made while the estate is in process of administration before the authorized fund is set up and in such case are clearly taxable. See *Matter of White* v. *Gilchrist*, 214 App. Div. 153, involving that question under the New York tax statute.

Section 213 (b) (3) should be construed as relating only to bequests of capital which have already been reached by Federal estate tax and as having no application to annuities paid from income. Otherwise, income from an estate which Congress intended to tax will escape taxation wholly and the provisions of Section 219 will be nullified.

II. The annuity constitutes taxable income to the respondent irrespective of whether she had received in annual payments an amount equal to the value of the bequest of the annuity on the date of the testator's death. The respondent made no investment of capital and relinquished no valuable rights in consideration of the receipt of the annuity. The cases relied upon by the respondent where annuities were purchased are distinguishable.

III. In view of the express provision of Section 219 that beneficiaries shall pay an income tax upon the income of estates distributed to them, the question as to whether double taxation will result is immaterial. *Hellmich* v. *Hellman*, 276 U. S. 233, 238. Moreover, no double taxation will result from the taxation to the beneficiary of such part of the income of the estate as is distributable to her. This tax will not fall upon the corpus of the estate, nor will the estate tax on the transfer of the net estate affect the annuity payable to the respondent.

ARGUMENT

I

ANNUITIES PAID OUT OF THE INCOME OF ESTATES CONSTITUTE TAXABLE INCOME TO THE RECIPIENTS UNDER THE REVENUE ACT OF 1921 AND ARE NOT EXEMPT AS BEQUESTS UNDER THAT ACT

Section 213 of the Revenue Act of 1921 (*infra*, pp. 29–30) provides:

> That for the purposes of this title * * * the term "gross income"—
>
> * * * * * *
>
> (b) Does not include the following items, which shall be exempt from taxation under this title:
>
> * * * * * *
>
> (3) The value of property acquired by gift, bequest, devise, or descent (but the income from such property shall be included in gross income).

We submit that the amount received by the respondent in the instant case was not exempt from taxation under this section, and that the present case is controlled by the decision of this Court in *Irwin* v. *Gavit*, 268 U. S. 161. There, as here, the income from an estate was paid to a beneficiary who acquired the right to receive it under the testator's will. The statute there involved was the Revenue Act of 1913 which, like the Revenue Act of 1921, laid a general tax upon income and contained an exemption of bequests. Section II, paragraph B, Act of October 3, 1913 (*infra*, p. 29). Both statutes make it clear that the income from bequests is not within the exemption.

The principal difference between the instant case and *Irwin* v. *Gavit* is that in the latter case the beneficiary had the right to receive a portion of the income only, while in this case the beneficiary has a right to receive certain annual payments with no restrictions as to whether they shall be paid from income or corpus. As a matter of fact, however, the residuary estate in this case was of sufficient size to produce the annuities and the annuity payments made to the beneficiary in the taxable year here involved were made from income earned by the residuary estate.

We think that this difference in the terms of the instrument giving the right is not material, that the principle of the *Gavit case* is equally applicable here, and that the income in this case, like that in the *Gavit case*, is income produced by the right

acquired under the will and therefore not exempt from taxation. The exemption in the Revenue Act of 1921, like that in the Revenue Act of 1913, does not extend to income, properly so called when distributed to a beneficiary. The same contention made here, that the income is exempt as a bequest, was made in the *Gavit case*. In rejecting that contention, this Court said (pp. 167–168):

> It seems to us hardly less clear that even if there were a specific provision that A should have no interest in the corpus, the payments would be income none the less, within the meaning of the statute and the Constitution, and by popular speech. In the first case it is true that the bequest might be said to be of the corpus for life, in the second it might be said to be of the income. *But we think that the provision of the act that exempts bequests assumes the gift of a corpus and contrasts it with the income arising from it, but was not intended to exempt income properly so-called simply because of a severance between it and the principal fund.* No such conclusion can be drawn from *Eisner* v. *Macomber*, 252 U. S. 189, 206, 207. The money was income in the hands of the trustees and we know of nothing in the law that prevented it being paid and received as income by the donee.
>
> The Courts below went on the ground that the gift to the plaintiff was a bequest and carried no interest in the corpus of the fund. We do not regard those considerations as conclusive, as we have said, but if it were

material *a gift of the income of a fund ordinarily is treated by equity as creating an interest in the fund.* Apart from technicalities we can perceive no distinction relevant to the question before us between a gift of the fund for life and a gift of the income from it. The fund is appropriated to the production of the same result whichever form the gift takes. * * * *But the distinction between the cases put of a gift from the corpus of the estate payable in instalments and the present seems to us not hard to draw, assuming that the gift supposed would not be income.* This is a gift from the income of a very large fund, as income. It seems to us immaterial that the same amounts might receive a different color from their source. (Italics ours.)

The same question arose in the case of *Heiner* v. *Beatty*, 17 F. (2d) 743 (C. C. A. 3d), which was affirmed *per curiam*, 276 U. S. 598, on the authority of *Irwin* v. *Gavit*, *supra*. In the *Beatty case* the testator provided for the payment of certain annuities to John W. Beatty and others, and directed his executor and trustee either (1) to set apart, hold in trust, invest, and keep invested in separate funds, one for each annuitant, sufficient sums to produce the several annuities, and to pay them from the interest and income of the respective funds in semi-annual payments, or (2) to purchase such annuities in life insurance companies. The executor and trustee adopted the first method of providing for the payment of the annuities. The Circuit Court of

Appeals for the Third Circuit held these annuities to be taxable and its decision was affirmed by this Court.

In this case the respondent did not receive a gift from the corpus of the estate payable in instalments. The record shows that in compliance with the provision of the will, the executors on December 30, 1920, permanently set aside to the residuary devisee and legatee, the James Gordon Bennett Memorial Home for New York Journalists Corporation, *"subject to taxes, annuities, and other charges"* (R. 14), certain assets in the amount of $3,133,260. The record shows that the total amount of annuities payable in 1920 was $144,000. (R. 13.) It is assumed that the same amount was payable each year, as the annuities were payable half-yearly from the time of the decedent's death. (R. 10.) The aggregate amount of the annuities paid during approximately three and one-half years from the time of the testator's death until November 30, 1921, was $485,675.31. (R. 34.) The bulk of the residuary estate was made up of promissory notes of a large corporation and bonds and mortgages on real estate. (R. 14.) Such a fund would normally produce sufficient income to satisfy the total annuity payments required and in this case it was found as a fact that in the year 1921 the annuities were paid from income actually produced by this fund. (R. 13.) Since annuities are payable primarily from income (*Delaney* v. *Van Aulen*, 84 N. Y. 16; *Matter of Kohler*, 193 App.

Div. 8, reversed on other grounds, 231 N. Y. 353; *Cummings* v. *Cummings*, 146 Mass. 501), there can be no doubt of the propriety of the payments made in this case.

Not only was the annuity properly paid from income, but it was undoubtedly the intention of the testator that it should be so paid, for the reason that he made a complete disposition of the corpus of his estate by the provision for establishing a charitable corporation.

Respondent is here claiming the benefit of an exemption. It is well settled that exemptions from taxation will be strictly construed. *Bank of Commerce* v. *Tennessee*, 161 U. S. 134, 136; *Heiner* v. *Colonial Trust Co.*, 275 U. S. 232. Since this exemption does not extend to bequests of income, respondent must show that a bequest of corpus was received. Irrespective of how the local law may regard an annuity, the Revenue Acts have their own criteria that look to certain rather severe tests of liability and exemption. *Weiss* v. *Wiener*, 279 U. S. 333. Furthermore, in *Irwin* v. *Gavit*, *supra*, this Court recognized that a bequest within the meaning of the exemption provision of the Revenue Act of 1913 did not include everything which might for other purposes be termed a bequest. Section 213 (b) (3) of the Revenue Act of 1921 is in substance the same as the exemption provision construed in *Irwin* v. *Gavit*, both exempting the value of property acquired by bequest but not the income derived therefrom.

This Court has held in *Towne* v. *Eisner*, 245 U. S. 418, that what in its nature is not income can not be made income merely by calling it such. As a necessary corollary it was indicated in *Irwin* v. *Gavit*, *supra*, that what is income in its nature can not be put beyond the reach of an income tax by handing it over to a beneficiary who has acquired the right to receive it under a will. It was there pointed out that the exemption provision of the statute exempts the gift of a corpus and that the exemption does not extend to the periodical receipt of income produced by the corpus.

It is not necessary to lay down a general rule here that will govern all cases. For present purposes it is sufficient that the money received by respondent was income in its nature, that the corpus was sufficiently large to provide income enough to satisfy the annuities, that there was nothing in the will which prevented the income being used for that purpose and that the testator is presumed to know the law that annuities are primarily paid out of income. Nor is it material that the annuity payments in other years were made from the corpus. (R. 13.) The respondent's tax for those other years is not involved in this case, and what *was* done here, not what might have been done, controls. *United States* v. *Phellis*, 257 U. S. 156, 173; *Miles* v. *Safe Deposit Co.*, 259 U. S. 247, 253; *Remington Rand, Inc.*, v. *Commissioner*, 33 F. (2d) 77, 78 (C. C. A. 2d), certiorari denied, 280 U. S. 591.

The intention of Congress not to permit any of the income of an estate or trust to escape taxation is made more manifest in the Revenue Act of 1921 than it was in the Revenue Act of 1913 construed in the *Gavit case.* No provision was made in the Act of 1913 to require the trustee or executor to pay an income tax on income received by him for the trust or the estate, but the scope of the later Acts was broadened to include such income. *Smietanka* v. *First Trust & Savgs. Bank,* 257 U. S. 602.

The intention of Congress with reference to the taxation or exemption of the annuities involved in this case can not be ascertained by construing Section 213 (b) (3) as an isolated provision, but requires an examination of other provisions. *Price* v. *Illinois,* 238 U. S. 446, 450. Section 219 is *in pari materia* with Section 213 (b) (3) and they must necessarily be construed together.

Section 219 (a) (*infra,* p. 30) provides that the tax imposed by Sections 210 and 211 shall apply to the income of estates or any kind of property held in trust, and subdivisions (1) and (4) specify that this provision relates to income received by estates of deceased persons during the period of administration or settlement of the estate and to income of estates and trusts which is to be distributed periodically, whether or not at regular intervals.

Under the remaining subdivisions of Section 219, income from such estates or trusts which is

distributable to a beneficiary is taxable to the beneficiary both during the period of administration of the estate and after administration is closed. In substance, Section 219 made an estate or trust a separate taxable entity to the end that all income produced by the corpus of an estate should be taxed even though there should be no beneficiary to receive it, but required the beneficiary to pay the tax on the portion of the income actually distributable to him.

So far as the beneficiary is concerned the test of taxability under this section is whether there is distributable to him net income of an estate or trust. That this is the proper test is recognized in the case of *Riker* v. *Commissioner*, 42 F. (2d) 150 (C. C. A. 2d). The question there involved was whether a residuary legatee was taxable upon income received from the estate in process of administration under the Revenue Act of 1921, the statute here involved. The taxpayer there argued that the payment received was an anticipated distribution of corpus and for that reason was not taxable. The court rejected that contention, holding that while the estate might not have been required to distribute any income to the beneficiary before final settlement, the amount received by the beneficiary was income to the estate and did not lose its character as such when distributed to the beneficiary. In that case, as in this, the sum in controversy was properly paid by the estate to the

beneficiary, though the decedent had not expressly provided for the payment of income.

In holding that the annuity paid to the respondent during 1921 was exempt from tax as a bequest, both the Board of Tax Appeals and the Circuit Court of Appeals distinguished the cases of *Irwin* v. *Gavit, supra,* and *Heiner* v. *Beatty, supra,* stating that in those cases the testator provided for the payment to the beneficiary of income from a particular trust fund, no amount being payable from the corpus of the trust, and that in the instant case no particular fund was set aside in trust for the payment of the annuities and they accordingly became a charge upon the corpus of the estate. One member of the Board dissented. (R. 21.)

In thus apparently distinguishing the case of a life beneficiary under a will who receives income in the form of a payment from a trust fund from one receiving similar income in the form of an annuity from a residuary estate, we believe that the Board of Tax Appeals and the Circuit Court of Appeals have relied too strongly upon technical distinctions between so-called "bequests of income" and "annuities" and in so doing have failed to consider whether these distinctions of form rather than substance can properly be given effect in interpreting the pertinent sections of the statute here involved.

That such technical distinctions are made is conceded. It is true that a bequest of income from a particular fund is payable only from income, where-

as an annuity is payable in all events, whether there be sufficient income or not, and in that sense is a charge on the corpus of the estate. *DeLaney* v. *Van Auten*, 84 N. Y. 16; *Matter of Dewey*, 153 N. Y. 63; *Matter of Gurnee*, 84 Misc. Rep. (N. Y.) 324, affirmed without opinion, 165 App. Div. 920, 214 N. Y. 660; *Whitson* v. *Whitson*, 53 N. Y. 479; *Peck* v. *Kinney*, 143 Fed. 76 (C. C. A. 2d). But matters of taxation are to be determined by substance rather than form (*United States* v. *Phellis*, 257 U. S. 156, 168; *Weiss* v. *Stearn*, 265 U. S. 242, 254; *Southern Pacific Co.* v. *Lowe*, 247 U. S. 330; *Saltonstall* v. *Saltonstall*, 276 U. S. 260; *Burk-Waggoner Assn.* v. *Hopkins*, 269 U. S. 110), and in substance there is no difference between payments which in fact are income, whether required to be paid as such or not. If one is not exempt as a bequest, it is difficult to see why the other should be.

If the existence of a fund from the income of which periodic payments are made is necessary to make the decision of *Irwin* v. *Gavit*, *supra*, applicable, it is pointed out that the annuity which has been taxed in the instant case was paid from a particular fund in the year 1921 here involved and in subsequent years. The intermediate account of settlement shows that on December 30, 1920, the executors permanently set aside to the residuary devisee and legatee the James Gordon Bennett Memorial Home for New York Journalists Corporation, *subject to taxes, annuities, and other charges*, certain assets in the amount of $3,133,260.

There was, moreover, implied authority in the will for the establishment of such a fund and the act of the executors was approved by the Surrogate's Court. The will directed the executors to retain and hold any personal property which might belong to the testator at the time of his death and to set it aside for the payment of any annuity and to sell or otherwise dispose of both real and personal property (with the exception of certain stock) for the purpose of paying annuities and other charges. Clearly, the will gave full authority to the executors to make any provision for the payment of the annuities which they deemed it advisable to make, and when they actually established a fund producing sufficient income to pay the annuities and paid them from it, no reason is suggested why Section 219 should not apply. In this connection it is pointed out that the will in the *Beatty case* did not set up a trust fund of a definite amount for the payment of the annuities but merely gave the executor and trustee authority to set apart and hold in trust sufficient sums to produce the annuity or in the alternative to purchase an annuity, but the Circuit Court of Appeals for the Third Circuit held that when the fund was subsequently established the income from it was taxable income to the beneficiary.

Moreover, we do not believe that the question whether a beneficiary should be taxed upon an annuity or any other income distributed periodically by an estate should be made to depend upon whether

a particular fund has been set aside. If no particular fund has been established, the entire estate including the income produced by it, is security for the payments.

That the test of taxability is not whether the income arises from a particular fund is made evident when consideration is given to the fact that even where the will directs the establishment of a fund sufficient to produce the payments of income to the beneficiary, payments may be made during the period of administration of the estate prior to the time when any fund provided for their payment may have been segregated from the assets of the estate. It would scarcely be argued that those payments would not be taxed because the fund had not yet been established.

That view was taken by the Appellate Division of the Supreme Court of New York in *Matter of White* v. *Gilchrist*, 214 App. Div. 153, which involved questions very similar to the questions here involved and arose under the income tax law of the State of New York. Section 359 of that law contains the same provision as to exemption of the value of property acquired by bequest as is involved here, and Section 365 contains provisions for the taxation of income from estates and trusts which are identical in all material respects with the provisions of Section 219 of the Revenue Act of 1921 here involved. The will in that case directed trustees to set aside a fund sufficient to produce certain annual income to be paid a designated beneficiary annually until she

should die or marry again. The executors and trustees failed to set up the fund. The court held the annuities to be taxable. An extract from the opinion in this case is printed as Appendix B, *infra*, pp. 34–35.

The record in the instant case does not show whether the estate was still in process of administration in 1921 and neither the Board nor the Circuit Court of Appeals appears to have considered that possibility. From our point of view the annuity is taxable whether paid from the income of the estate during the period of administration or paid after administration was closed.

The record shows the filing of an intermediate account of settlement but does not show that a judicial settlement was made in accordance with Section 2727 or Section 2729 of the Code of Civil Procedure of New York. The intermediate account which was filed showed that all remaining assets had been permanently set aside for the residuary devisee and legatee, subject to the payment of annuities. The fund thus set aside was held in trust by the executors for the payment of annuities, which they paid out of income. *Matter of Dewey*, 153 N. Y. 63; *Ward* v. *Ward*, 105 N. Y. 68; *Matter of Kohler*, 231 N. Y. 353; *Matter of Zeigler*, 218 N. Y. 544; *Johnson* v. *Lawrence*, 95 N. Y. 154; *Matter of Slocum*, 169 N. Y. 153.

For the foregoing reasons it is believed that the Circuit Court of Appeals erred in construing Section 213 (b) (3) as applicable to annuities paid

from income. So to construe that provision will have the effect of nullifying the provisions of Section 219 and will thus violate the rule that statutes should be so construed, if practicable, that one section will explain and support and not defeat or destroy another section. *Bernier* v. *Bernier*, 147 U. S. 242, 246. We submit that this construction of the statute made by the petitioner will serve to eliminate all possible conflict between Section 213 (b) (3) and Section 219, and to give a sensible and intelligent effect to each.

It is pointed out that the practical effect of the decision below is to enable income of an estate which arises from non-exempt sources to escape taxation altogether. Clearly, the fiduciary can not be taxed upon such income, for under Section 219 (d) of the Act the fiduciary, whether executor or trustee, is not to pay the tax upon income which is distributed to beneficiaries. If such income may not be taxed to the beneficiaries on the theory that it represents a bequest, it is not taxed at all.

II

THE ANNUITY CONSTITUTES TAXABLE INCOME TO THE RESPONDENT IRRESPECTIVE OF WHETHER SHE HAD PREVIOUSLY RECEIVED IN ANNUAL PAYMENTS AN AMOUNT EQUAL TO THE VALUE OF THE BEQUEST OF THE ANNUITY ON THE DATE OF THE TESTATOR'S DEATH.

In her brief in the Circuit Court of Appeals (p. 21) the respondent urged that a gift or bequest of an annuity is indistinguishable from a pur-

chased annuity, which does not produce taxable income until the cost or value has been recovered. The cases of *Allen* v. *Brandeis*, 29 F. (2d) 363 (C. C. A. 8th), *Warner* v. *Walsh*, 27 F. (2d) 952 (D. Conn.), and *United States* v. *Bolster*, 26 F. (2d) 760 (C. C. A. 1st), were cited. See also *Warner* v. *Walsh*, 15 F. (2d) 367 (C. C. A. 2d), and *Logan* v. *Commissioner*, 42 F. (2d) 193 (C. C. A. 2d), now pending before this Court on a writ of certiorari, No. 521, October Term, 1930.

In each of the cases cited by the respondent the taxpayer elected to accept annuities in lieu of dower or similar statutory rights in the estate of the decedent. Under those facts it was held that the waiver of the statutory rights constituted a valuable consideration paid for the annuities and hence that the annuities would not be taxable until there had been a return of capital.

In the *Bolster case, supra,* the Circuit Court of Appeals for the First Circuit emphasized the difference between the question involved in that case and the question involved in the case of *Heiner* v. *Beatty*, 17 F. (2d) 73 (C. C. A. 3rd), affirmed in *Beatty* v. *Heiner*, 276 U. S. 598, which is relied upon by the petitioner as being analogous to the present case. The court said (p. 763):

> In *Heiner* v. *Beatty, supra,* it was contended that income received by the taxpayer under the will of the decedent was exempt

from taxation because that income constituted a "bequest." In the instant case the ground of the exemption is, not that the income received is a bequest but that such income is exempt, because it represents "purchase money" or a return of capital. In that case the record disclosed facts similar to those in *Irwin* v. *Gavit, supra.*

The facts in the present case show that the taxpayer received, as an annuity, income from the decedent's estate as the consequence of a gift and not as the result of the investment of a capital sum or the relinquishment of any valuable rights. There was consequently no part of the annuities which represented a return of capital. The case in that respect is analogous to the case of *Heiner* v. *Beatty, supra.* Attention is called to the fact that in the *Beatty case* the executors were given the authority, in the alternative, to purchase an annuity for the beneficiary, and it appears from the opinion in that case, that the annuity payments likewise would have been taxed as income to the beneficiary, even if the annuity had been purchased by the executors under their alternative power. The important consideration in that, as well as in the present case, is that the annuitant contributed no purchase price, incurred no cost, and invested no capital sum to the return of which she was entitled before taxable income arose.

III

NO QUESTION OF DOUBLE TAXATION IS INVOLVED

The respondent urged in the court below that double taxation will result from the petitioner's construction of the Act because of the Federal estate tax levied upon the transfer of the net estate of James Gordon Bennett. The Circuit Court of Appeals (R. 41) assumed, "if material," that all of the annuities were subject to the estate tax so that to sustain this construction would involve double taxation and cited *United States* v. *Supplee-Biddle Co.*, 265 U. S. 189, 196, holding that double taxation is a result "to be avoided unless required by express words."

But it is precisely because Section 219 of the Revenue Act of 1921 does expressly require that beneficiaries of estates and trusts shall pay an income tax upon the income of estates distributed to them periodically that the question as to whether double taxation may result is immaterial. In *Hellmich* v. *Hellman*, 276 U. S. 233, this Court said (p. 238):

> When, as here, Congress has clearly expressed its intention, the statute must be sustained even though double taxation results.

While the question of double taxation is, therefore, immaterial, we submit that no double taxa-

tion will result from the taxation of the annuity as income in this case. The estate tax is levied upon the transfer of the net estate of the decedent and is based upon the value of the net estate. Revenue Act of 1916, c. 463, sec. 201, 39 Stat. 756. Such a tax upon transfers, measured by the value of the net estate, has no relation to the annuities. The income here involved was not a part of the corpus of the estate on which the estate tax was levied.

In the court below respondent argued that where the testator provides for the payment of annuities as a charge upon his entire estate with the residuum to a charitable organization, the value of the net taxable estate includes the value of the annuities as of the date of death and in that connection referred to Article 15 of Treasury Regulations 63, providing for the valuation of annuities by mortality tables in determining the value of the net estate for Federal estate tax purposes. But the regulations referred to only relate to the valuation of an annuity which was payable to the decedent for a period of years or for the life of another. An annuity created by the will of the testator is not valued for Federal estate tax purposes, and the regulation referred to has no bearing on this case.

CONCLUSION

The judgment below is erroneous and should be reversed.

Respectfully submitted.

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JANUARY, 1931.

APPENDIX A

STATUTES AND REGULATIONS INVOLVED

STATUTES

Section II, Paragraph (B) of the Act of October 3, 1913, c. 16, 38 Stat. 114, 167, provides in part as follows:

> B. That, subject only to such exemptions and deductions as are hereinafter allowed, the net income of a taxable person shall include gains, profits, and income derived from salaries, wages, or compensation for personal service of whatever kind and in whatever form paid, or from professions, vocations, businesses, trade, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in real or personal property, also from interest, rent, dividends, securities, or the transaction of any lawful business carried on for gain or profit, or gains or profits and income derived from any source whatever, including the income from but not the value of property acquired by gift, bequest, devise, or descent: * * *.

The Revenue Act of 1921, c. 136, 42 Stat. 227, 237, 246, provides in part:

> SEC. 213. That for the purposes of this title * * * the term "gross income"—
>
> (a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever

kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * but

(b) Does not include the following items, which shall be exempt from taxation under this title:

* * * * *

(3) The value of property acquired by gift, bequest, device, or descent (but the income from such property shall be included in gross income);

* * * * *

SEC. 219. (a) That the tax imposed by sections 210 and 211 shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income received by estates of deceased persons during the period of administration or settlement of the estate;

* * * * *

(4) Income which is to be distributed to the beneficiaries periodically, whether or not at regular intervals, and the income collected by a guardian of an infant to be held or distributed as the court may direct.

(b) The fiduciary shall be responsible for making the return of income for the estate or trust for which he acts. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that (in lieu of the deduction authorized by paragraph (11) of subdivision (a) of section 214) there shall also

be allowed as a deduction, without limitation, any part of the gross income which, pursuant to the terms of the will or deed creating the trust, is during the taxable year paid or permanently set aside for the purposes and in the manner specified in paragraph (11) of subdivision (a) of section 214. In cases in which there is any income of the class described in paragraph (4) of subdivision (a) of this section the fiduciary shall include in the return a statement of the income of the estate or trust which, pursuant to the instrument or order governing the distribution, is distributable to each beneficiary, whether or not distributed before the close of the taxable year for which the return is made.

(c) In cases under paragraphs (1), (2), or (3) of subdivision (a) or in any other case within subdivision (a) of this section, except paragraph (4) thereof the tax shall be imposed upon the net income of the estate or trust and shall be paid by the fiduciary, except that in determining the net income of the estate of any deceased person during the period of administration or settlement there may be deducted the amount of any income properly paid or credited to any legatee, heir, or other beneficiary. * * *

(d) In cases under paragraph (4) of subdivision (a), and in the case of any income of an estate during the period of administration or settlement permitted by subdivision (c) to be deducted from the net income upon which tax is to be paid by the fiduciary, the tax shall not be paid by the fiduciary, but there shall be included in computing the net income of each beneficiary that part of the income of the estate or trust for its taxable year which, pursuant to the instrument or

order governing the distribution, is distributable to such beneficiary, whether distributed or not, or, if his taxable year is different from that of the estate or trust, then there shall be included in computing his net income his distributive share of the income of the estate or trust for its taxable year ending within the taxable year of the beneficiary. * * *

(e) In the case of an estate or trust the income of which consists both of income of the class described in paragraph (4) of subdivision (a) of this section and other income, the net income of the estate or trust shall be computed and a return thereof made by the fiduciary in accordance with subdivision (b) and the tax shall be imposed, and shall be paid by the fiduciary in accordance with subdivision (c), except that there shall be allowed as an additional deduction in computing the net income of the estate or trust that part of its income of the class described in paragraph (4) of subdivision (a) which, pursuant to the instrument or order governing the distribution, is distributable during its taxable year to the beneficiaries. In cases under this subdivision there shall be included, as provided in subdivision (d) of this section, in computing the net income of each beneficiary, that part of the income of the estate or trust which, pursuant to the instrument or order governing the distribution, is distributable during the taxable year to such beneficiary.

REGULATIONS

Treasury Regulations 62 provide in part as follows:

ART. 73. *Gifts and bequests.*—Money and real or personal property received as gifts, or received under a will or under statutes of

descent and distribution, are exempt from tax, although the income therefrom derived from investment, sale, or otherwise is not. * * *

ART. 343. *Decedent's estate during administration.*—The "period of administration or settlement of the estate" is the period required by the executor or administrator to perform the ordinary duties pertaining to administration, in particular the collection of assets and the payment of debts and legacies. It is the time actually required for this purpose, whether longer or shorter than the period specified in the local statute for the settlement of estates. Where an executor, who is also named as trustee, fails to obtain his discharge as executor, the period of administration continues up to the time when the duties of administration are complete and he actually assumes his duties as trustee, whether pursuant to an order of the court or not. * * *

ART. 345. *Estates and trusts taxed to beneficiaries.*—In the case of (a) a trust the income of which is distributable periodically, (b) an ordinary guardianship of a minor, and (c) an estate of a decedent before final settlement as to any income properly paid or credited as such to a beneficiary, the income is taxable directly to the beneficiary or beneficiaries. Each such beneficiary must include in his return his distributive share of the net income, even though not yet paid him, but if his taxable year is different from that of the estate or trust, then he need only include in computing his net income his distributive share of the income of the estate or trust for its taxable year ending within his taxable year. The regulations governing partnerships are generally applicable to such an estate or trust.

APPENDIX B

In *Matter of White* v. *Gilchrist*, 214 App. Div. 153, 155–156, the court said:

> We think that, under the holding of the United States Supreme Court, the claim of the petitioner herein can not be sustained, namely, that as to her the annual payments constituted a "legacy" not subject to income tax under that provision of the law (Tax Law § 359, subd. 2, ¶c, as added by Laws of 1919, chap. 627) which excludes from gross income "the value of property acquired by * * * bequest." The executors were appointed trustees by the will and th[illegible] were likewise made the residuary legatees and devisees. The executors have never accounted although ordered to do so in 1916 and it appears that the direction of the will that a fund should be set apart sufficient to produce an annual income of $10,000 has never been carried out. The record shows, however, that for the three tax years involved here the income of the estate in their hands has been more than adequate to pay the $10,000 annually. The sum involved is thus income to the estate and the executors have each year made a fiduciary return to the Tax Commission to the effect that the payment to the petitioner has been made out of income of the estate. The mere fact that the executors and trustees have not obeyed the will of the testator by setting apart the trust fund directed by the will does not change the character of the thing received by the petitioner.

The executors concededly have not trenched upon the corpus but have turned over nothing but income of the estate. Potentially the whole estate not otherwise specifically disposed of by the will was chargeable with this trust until the trust fund was set apart as required by the will. The testator did not provide for a large legacy payable in fractions out of the corpus of the estate but he treated it as income and separately disposed of the corpus of the fund out of which it was to be paid, to take effect at the death or remarriage of petitioner. It is unnecessary for us to decide whether the petitioner will ever get anything from this estate or trust which is not income to the estate or trust. It affirmatively appears that the payments now in question were income of the estate or trust. These payments not being within the "legacy" exemption of the Income Tax Law but income, according to common understanding and judicial definition, are taxable under the act. Moreover, the mere fact that the intangible interest of petitioner was described as an "annuity" and its capitalized value was fixed for inheritance tax purposes in 1911, the tax upon which was paid by the petitioner, does not make these annual payments exempt from income tax. This worked no change in the real character of the payments and the State is not estopped.

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